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MONTANA UNIVERSITY SYSTEM-  
WORKERS' COMPENSATION PROGRAM

AUDITED FINANCIAL STATEMENTS  
With Supplemental Information

June 30, 2009 and 2008

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Junkermier • Clark  
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December 1, 2009

To the Committee  
Montana University System –  
Workers' Compensation Program  
P.O. Box 203201  
Helena, Montana 59620-3201

We have audited the financial statements of the business-type activities of Montana University System – Workers' Compensation Program for the year ended June 30, 2009. Professional standards require that we provide you with information about our responsibilities under generally accepted auditing standards, and *Government Auditing Standards*, as well as certain information related to the planned scope and timing of our audit. We have communicated such information in our letter to you dated July 13, 2009. Professional standards also require that we communicate to you the following information related to our audit.

### **Significant Audit Findings**

#### ***Qualitative Aspects of Accounting Policies***

Management has the responsibility for selection and use of appropriate accounting policies. The significant accounting policies used by Montana University System - Workers' Compensation Program, are described in Note 1 to the financial statements. No new accounting policies were adopted and the application of existing policies was not changed during the fiscal year ended June 30, 2009. We noted no transactions entered into by the Program during the year for which there is a lack of authoritative guidance or consensus. All significant transactions have been recognized in the financial statements in the proper period.

Accounting estimates are an integral part of the financial statements prepared by management and are based on management's knowledge and experience about past and current events and assumptions about future events. Certain accounting estimates are particularly sensitive because of their significance to the financial statements and because of the possibility that future events affecting them may differ significantly from those expected. The most sensitive estimate affecting the financial statements was the estimated claims liability.

Management's estimate of the claims estimate is based on an actuarial calculation performed by Milliman, Inc., the Program's consulting actuaries. We evaluated the key factors and assumptions used to develop the estimated claims liability in determining that it is reasonable in relation to the financial statements taken as a whole.



To the Committee  
Montana University System - Workers' Compensation Program  
December 1, 2009

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### ***Difficulties Encountered in Performing the Audit***

We encountered no significant difficulties in dealing with management in performing and completing our audit.

### ***Corrected and Uncorrected Misstatements***

Professional standards require us to accumulate all known and likely misstatements identified during the audit, other than those that are trivial, and communicate them to the appropriate level of management. Management has corrected all such misstatements. In addition, none of the misstatements detected as a result of audit procedures and corrected by management were material, either individually or in the aggregate, to the financial statements taken as a whole.

### ***Disagreements with Management***

For purposes of this letter, professional standards define a disagreement with management as a financial accounting, reporting, or auditing matter, whether or not resolved to our satisfaction, that could be significant to the financial statements or the auditor's report. We are pleased to report that no such disagreements arose during the course of our audit.

### ***Management Representations***

We have requested certain representations from management that are included in the management representation letter dated December 1, 2009.

### ***Management Consultations with Other Independent Accountants***

In some cases, management may decide to consult with other accountants about auditing and accounting matters, similar to obtaining a "second opinion" on certain situations. If a consultant involves application of an accounting principle to the Organization's financial statements or a determination of the type of auditor's opinion that may be expressed on those statements, our professional standards require the consulting accountant to check with us to determine that the consultant has all the relevant facts. To our knowledge, there were no such consultations with other accountants.

### ***Other Audit Findings or Issues***

We generally discuss a variety of matters, including the application of accounting principles and auditing standards, with management each year prior to retention as the Program's auditors. However, these discussions occurred in the normal course of our professional relationship and our responses were not a condition to our retention.



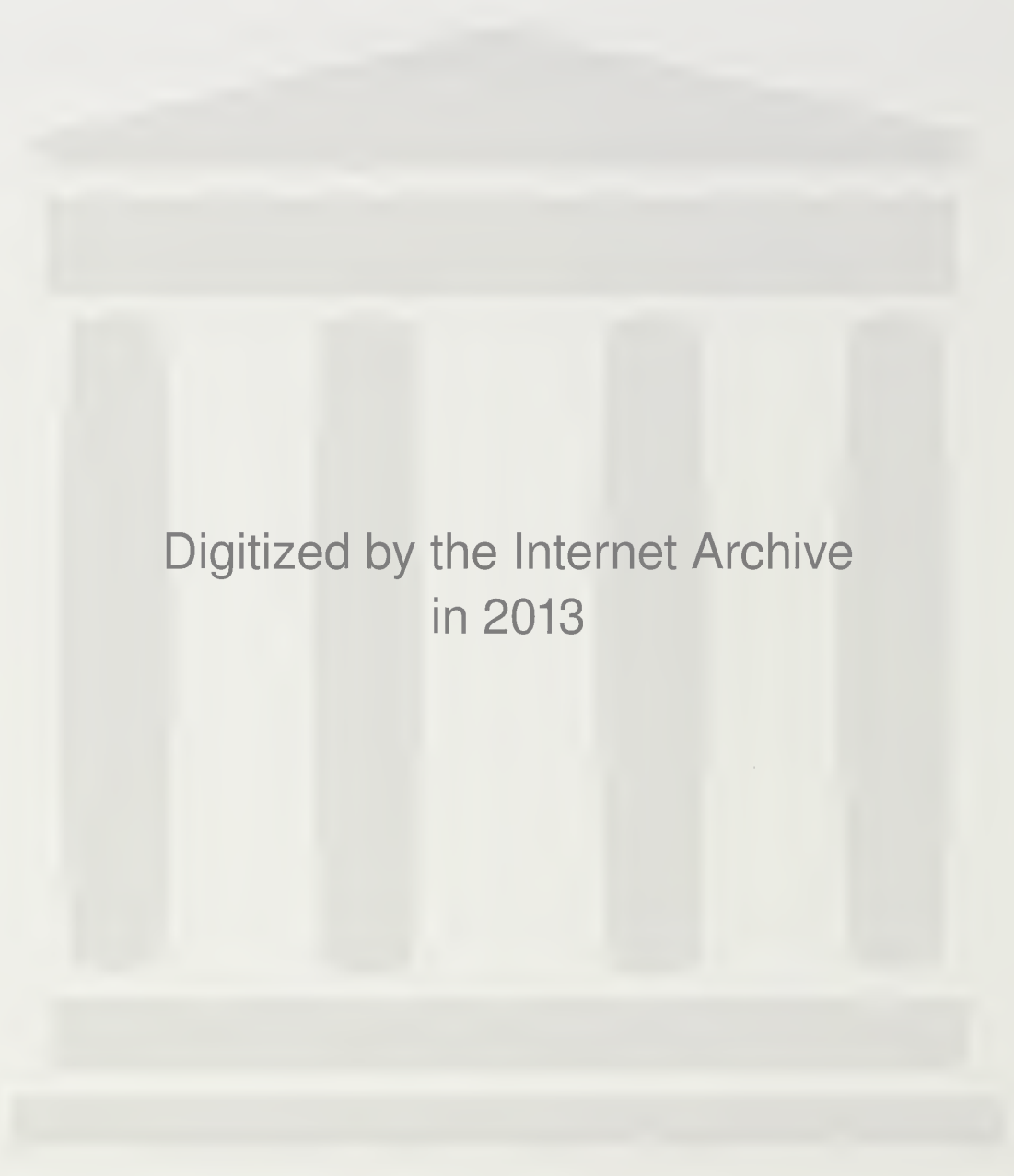
To the Committee  
Montana University System - Workers' Compensation Program  
December 1, 2009

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This information is intended solely for the use of the Committee and management of Montana University System - Workers' Compensation Program, and is not intended to be and should not be used by anyone other than these specified parties.

*Junkermier, Clark, Campanella, Stevens, PC*

Helena, Montana



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**MONTANA UNIVERSITY SYSTEM -  
WORKERS' COMPENSATION PROGRAM**

**AUDITED FINANCIAL STATEMENTS  
With Supplemental Information**

**June 30, 2009 and 2008**



# LEGISLATIVE AUDIT DIVISION

Tori Hunthausen, Legislative Auditor  
Monica Huyg, Legal Counsel



Deputy Legislative Auditors:  
James Gillett  
Angie Grove

November 2009

The Legislative Audit Committee  
of the Montana State Legislature:

Enclosed is the report on the audit of the Montana University System Workers' Compensation Program for the fiscal year ended June 30, 2009.

The audit was conducted by Junkermier, Clark, Campanella, Stevens, P.C., under a contract between the firm and our office. The comments and recommendations contained in this report represent the views of the firm and not necessarily the Legislative Auditor.

The agency's written response to the report recommendations is included in the back of the audit report.

Respectfully submitted,

A handwritten signature in cursive script, appearing to read "Tori Hunthausen", is written over a horizontal line.

Tori Hunthausen, CPA  
Legislative Auditor

Enc.

09C-04



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WORKERS' COMPENSATION PROGRAM  
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## INDEPENDENT AUDITORS' REPORT

To the Committee  
Montana University System -  
Workers' Compensation Program  
Helena, Montana

We have audited the accompanying financial statements of the Montana University System - Workers' Compensation Program (an enterprise fund of the State of Montana) as of and for the years ended June 30, 2009 and 2008, as listed in the table of contents. These financial statements are the responsibility of the Montana University System - Workers' Compensation Program's management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinions.

As discussed in Note 1, the financial statements present only the Montana University System - (Workers' Compensation Program) and do not purport to, and do not, present fairly the financial position of the State of Montana as of June 30, 2009 and 2008, and the changes in its financial position, or, where applicable, its cash flows for the year then ended in conformity with accounting principles generally accepted in the United States of America.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Montana University System - Workers' Compensation Program (an enterprise fund of the State of Montana) as of June 30, 2009 and 2008 and the changes in financial position and cash flows thereof for the year then ended in conformity with accounting principles generally accepted in the United States of America.



In accordance with *Government Auditing Standards*, we have also issued our report dated December 1, 2009, on our consideration of Montana University System - Workers' Compensation Program's internal control over financial reporting and our tests of its compliance with laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing and not to provide an opinion on the internal control over financial reporting or on compliance. The report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in conjunction with this report in considering the results of our audit.

Montana University System - Workers' Compensation Program has not presented the management's discussion and analysis that accounting principles generally accepted in the United States has determined is necessary to supplement, although not required to be part of, the basic financial statements.

The claims development information on page 14 is not a required part of the basic financial statements but is supplementary information required by accounting principles generally accepted in the United States of America. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the supplementary information. However, we did not audit the information and express no opinion on it.

***Junkermier, Clark, Campanella, Stevens, P.C.***

Helena, Montana  
December 1, 2009



**MONTANA UNIVERSITY SYSTEM -  
WORKERS' COMPENSATION PROGRAM  
STATEMENTS OF NET ASSETS**

|                                                         | <b>June 30</b>              |                             |
|---------------------------------------------------------|-----------------------------|-----------------------------|
|                                                         | <b>2009</b>                 | <b>2008</b>                 |
| <b>ASSETS</b>                                           |                             |                             |
| <b>Current Assets</b>                                   |                             |                             |
| Cash and cash equivalents                               | \$ 12,233,511               | \$ 9,352,302                |
| Interest receivable                                     | 7,566                       | 13,132                      |
| Other receivables                                       | -                           | 94                          |
| Due from component units                                | 382,089                     | 374,835                     |
| Short-term securities lending collateral                | 815,681                     | 395,055                     |
| Prepaid expense                                         | 243,015                     | 249,921                     |
| Total current assets                                    | <u>13,681,862</u>           | <u>10,385,339</u>           |
| <b>Noncurrent Assets</b>                                |                             |                             |
| Long-term investments                                   | <u>1,034,213</u>            | <u>840,306</u>              |
| Total noncurrent assets                                 | <u>1,034,213</u>            | <u>840,306</u>              |
| Total assets                                            | <u><u>\$ 14,716,075</u></u> | <u><u>\$ 11,225,645</u></u> |
| <b>LIABILITIES</b>                                      |                             |                             |
| <b>Current Liabilities</b>                              |                             |                             |
| Vouchers payable                                        | \$ 59,428                   | \$ 17,154                   |
| Due to other funds                                      | 129,399                     | 160                         |
| Due to component unit                                   | 39                          | 63                          |
| Current portion of compensated absences liability       | 3,196                       | 3,461                       |
| Current securities lending liability                    | 815,681                     | 395,055                     |
| Current portion of estimated claims liability           | 994,785                     | 855,695                     |
| Total current liabilities                               | <u>2,002,528</u>            | <u>1,271,588</u>            |
| <b>Noncurrent Liabilities</b>                           |                             |                             |
| Compensated absences liability - net of current portion | 3,998                       | 1,442                       |
| Estimated claims liability-net of current portion       | 6,738,215                   | 5,501,305                   |
| Estimated liability - OPEB                              | 4,789                       | 2,345                       |
| Total noncurrent liabilities                            | <u>6,747,002</u>            | <u>5,505,092</u>            |
| Total liabilities                                       | <u><u>\$ 8,749,530</u></u>  | <u><u>\$ 6,776,680</u></u>  |
| <b>NET ASSETS</b>                                       |                             |                             |
| Unrestricted Net Assets                                 | <u><u>\$ 5,966,545</u></u>  | <u><u>\$ 4,448,965</u></u>  |

See the notes to financial statements.



**MONTANA UNIVERSITY SYSTEM -  
WORKERS' COMPENSATION PROGRAM  
STATEMENTS OF REVENUES, EXPENSES AND CHANGES IN NET ASSETS**

|                                         | <b>Years ended June 30</b> |              |
|-----------------------------------------|----------------------------|--------------|
|                                         | <b>2009</b>                | <b>2008</b>  |
| <b>OPERATING REVENUES</b>               |                            |              |
| Premiums                                | \$ 5,003,315               | \$ 4,659,752 |
| <b>OPERATING EXPENSES</b>               |                            |              |
| Claims administration                   | 222,313                    | 152,131      |
| Actuary fees                            | 16,500                     | 15,482       |
| Consulting & Professional Services      | 31,349                     | 7,077        |
| Insurance and reinsurance expense       | 240,712                    | 220,378      |
| Audit fees                              | 9,500                      | 9,500        |
| Dues                                    | 2,800                      | 3,110        |
| Department of Labor assessment          | 46,613                     | 43,808       |
| Bank Service Charges                    | 88                         | 140          |
| Office supplies, printing, postage      | 309                        | 298          |
| Salaries, payroll taxes and benefits    | 83,686                     | 80,590       |
| Telephone                               | 716                        | 723          |
| Miscellaneous expense                   | 46,450                     | 38,083       |
| Claims paid and claims expense          | 2,974,436                  | 2,512,057    |
| Total operating expenses                | 3,675,472                  | 3,083,377    |
| <b>OPERATING INCOME</b>                 | 1,327,843                  | 1,576,375    |
| <b>NONOPERATING REVENUES (EXPENSES)</b> |                            |              |
| Interest and investment income          | 167,866                    | 337,725      |
| Other nonoperating income               | 21,871                     | 5,768        |
| Amortization of bond issuance cost      | -                          | (9,235)      |
| Bond interest expense                   | -                          | (10,535)     |
| Trustee fees                            | -                          | (2,000)      |
| Other Debt Service Charges              | -                          | (2,752)      |
| Total nonoperating revenues (expenses)  | ,189,737                   | ,318,971     |
| <b>CHANGE IN NET ASSETS</b>             | 1,517,580                  | 1,895,346    |
| <b>NET ASSETS BEGINNING OF YEAR</b>     | 4,448,965                  | 2,553,619    |
| <b>NET ASSETS END OF YEAR</b>           | \$ 5,966,545               | \$ 4,448,965 |

See the notes to financial statements.



**MONTANA UNIVERSITY SYSTEM -  
WORKERS' COMPENSATION PROGRAM  
STATEMENTS OF CASH FLOWS**

|                                                               | <b>Years ended June 30</b> |                     |
|---------------------------------------------------------------|----------------------------|---------------------|
|                                                               | <b>2009</b>                | <b>2008</b>         |
| <b>CASH FLOWS FROM OPERATING ACTIVITIES</b>                   |                            |                     |
| Cash received from premiums:                                  | 4,996,155                  | \$ 4,454,176        |
| Claims paid and claims expense                                | (1,568,128)                | (1,658,057)         |
| Cash payments for insurance and reinsurance expense           | (233,806)                  | (470,299)           |
| Cash payments for employees                                   | (81,395)                   | (75,687)            |
| Cash payments for administrative expenses                     | (187,894)                  | (301,723)           |
| Cash payments for other operating expenses                    | <u>(45,119)</u>            | <u>(36,899)</u>     |
| Net cash provided by operating activities                     | <u>2,879,813</u>           | <u>1,911,511</u>    |
| <b>CASH FLOWS (USED) FROM NONCAPITAL FINANCING ACTIVITIES</b> |                            |                     |
| Cash paid for interest                                        | -                          | (12,074)            |
| Cash paid for trustee fees and other debt service charges     | -                          | (4,752)             |
| Principal paid on bonds                                       | <u>-</u>                   | <u>(430,000)</u>    |
| Net cash (used) by noncapital financing activities            | <u>-</u>                   | <u>(446,826)</u>    |
| <b>CASH FLOWS (USED) FROM INVESTING ACTIVITIES</b>            |                            |                     |
| Proceeds from sale of investments                             | -                          | 650,263             |
| Reclassification of STIP to investments                       | (193,907)                  | (840,306)           |
| Other nonoperating income                                     | 21,871                     | 5,768               |
| Interest received                                             | <u>173,432</u>             | <u>340,905</u>      |
| Net cash from investing activities                            | <u>1,396</u>               | <u>156,630</u>      |
| Net increase in cash                                          | 2,881,209                  | 1,621,315           |
| <b>CASH BEGINNING OF YEAR</b>                                 | <u>9,352,302</u>           | <u>7,730,987</u>    |
| <b>CASH END OF YEAR</b>                                       | <u>\$ 12,233,511</u>       | <u>\$ 9,352,302</u> |

See the notes to financial statements.



**MONTANA UNIVERSITY SYSTEM -  
WORKERS' COMPENSATION PROGRAM  
STATEMENTS OF CASH FLOWS (Continued)**

**RECONCILIATION OF OPERATING INCOME TO NET CASH PROVIDED BY OPERATING  
ACTIVITIES**

|                                                                                            | <b>Years ended June 30</b> |                     |
|--------------------------------------------------------------------------------------------|----------------------------|---------------------|
|                                                                                            | <b>2009</b>                | <b>2008</b>         |
| Operating Income                                                                           | \$ 1,327,843               | \$ 1,576,375        |
| Adjustments to reconcile operating income to net cash provided by<br>operating activities: |                            |                     |
| (Increase) in other receivables                                                            | 94                         | (94)                |
| (Increase) decrease in due from component units                                            | (7,254)                    | (205,482)           |
| (Increase) decrease in prepaid expense                                                     | 6,906                      | (249,921)           |
| (Decrease) increase in vouchers payable                                                    | 42,274                     | (11,532)            |
| (Decrease) increase in other accrued expenses                                              | -                          | (25,275)            |
| Increase in due to other funds                                                             | 129,239                    | (33,871)            |
| Increase in due to component unit                                                          | (24)                       | 63                  |
| Increase in compensated absences liability                                                 | 2,291                      | 4,903               |
| Increase in estimated liability - OPEB                                                     | 2,444                      | 2,345               |
| Increase in estimated claims liability                                                     | <u>1,376,000</u>           | <u>854,000</u>      |
|                                                                                            | <u>1,551,970</u>           | <u>335,136</u>      |
| Net cash provided by operating activities                                                  | <u>\$ 2,879,813</u>        | <u>\$ 1,911,511</u> |

**SCHEDULE OF NONCASH INVESTING, CAPITAL, AND FINANCING ACTIVITIES**

|                                                  | <b>Years ended June 30</b> |                  |
|--------------------------------------------------|----------------------------|------------------|
|                                                  | <b>2009</b>                | <b>2008</b>      |
| Increase (decrease) in fair value of investments | <u>\$ -</u>                | <u>\$ 20,623</u> |
| Amortization of bond issuance costs              | <u>\$ -</u>                | <u>\$ 9,235</u>  |

See the notes to financial statements.



**MONTANA UNIVERSITY SYSTEM -  
WORKERS' COMPENSATION PROGRAM  
NOTES TO FINANCIAL STATEMENTS  
June 30, 2009 and 2008**

**1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

***Organization and Description of Program:***

The Montana University System - Workers' Compensation Program (the Program) was organized to provide self-insured workers' compensation coverage for employees of the Montana University System. The Montana University System Board of Regents elected to provide workers' compensation coverage under the Compensation Plan Number One (MCA 39-71-2101) as of July 1, 2003. Prior to that date, the Montana University System obtained its workers' compensation coverage through participation in the State Fund. Each member of the Program is jointly and severally liable for the full amount of any and all known or unknown claims of each member arising during the member's participation in the program.

In order to fund an initial reserve for self-insured claims, the Montana University System issued \$2,050,000 Series 2003 Workers' Compensation Program Revenue Bonds, all of which have been repaid as of June 30, 2008.

***Administration of Claim Payments:***

The Program's contract with Missoula County Workers' Compensation Group Insurance Authority terminated in June 2007. Missoula County Workers' Compensation Group Insurance Authority has assigned its contract for claims administration services with Intermountain Claims, Inc., to the Montana University System-Workers Compensation Program. Montana University System-Workers Compensation Program contracts directly with Intermountain Claims, Inc. for claim administration services in June 2008.

***Basis of Accounting:***

The Program has adopted the provisions of GASB Statement 10 (as amended by GASB Statement No. 30 and GASB Interpretation No. 4), under those provisions, the Program utilizes accounting principles applicable to public entity risk pools. The Program's financial statements are presented on the accrual basis of accounting. Revenues are recognized when they are earned, and expenses are recognized when they are incurred. Operating revenues and expenses generally arise from providing insurance coverage. All other revenues and expenses are classified as nonoperating. The Program has elected to apply the provisions of applicable pronouncements issued by the Financial Accounting Standards Board and the AICPA prior to November 30, 1989, except those that conflict with or contradict GASB pronouncements. Government entities have the option of whether or not to apply FASB pronouncements issued after that date to their proprietary activities. In accordance with GASB Statement No. 20, management has elected not to apply FASB pronouncements issued after November 30, 1989.

***Reporting Entity:***

The Program is considered a public entity risk pool and is reported as an enterprise fund of the State of Montana. In accordance with governmental accounting and financial reporting standards there are no component units to be included with the Montana University System-Workers Compensation Program as a reporting agency.

***Bad Debts:***

The Program considers all premium receivables to be collectible.



**MONTANA UNIVERSITY SYSTEM -  
WORKERS' COMPENSATION PROGRAM  
NOTES TO FINANCIAL STATEMENTS (Continued)  
June 30, 2009 and 2008**

**1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)**

***Investments:***

The Program is authorized to invest in the Short Term Investment Pool (STIP) which is administered by the State of Montana Board of Investments. The STIP portfolio includes asset-backed securities, banker's acceptances, certificates of deposit, corporate and government securities, repurchase agreements and variable-rate (floating-rate) instruments. Asset-backed securities represent debt securities collateralized by a pool of non-mortgage assets such as trade and loan receivables, equipment leases, and credit cards. Variable-rate (floating-rate) securities pay a variable rate of interest until maturity. The variable-rate securities float with the 91 day treasury bill or LIBOR (London Interbank Offered Rate).

***Restricted Cash and Investments:***

The trust indenture for the Series 2003 Workers' Compensation Revenue Bonds requires that each month program revenues be set aside in a debt service account to be used for the payment of interest and principal. The trust indenture requirement was satisfied in May 2008 when the Series 2003 Worker's Compensation Revenue Bonds were retired.

The Trust indenture for the Series 2003 Workers' Compensation Revenue Bonds requires that funds deposited into a bank-administered trust fund be invested in tax-exempt obligations. The Series 2003 Worker's Compensation Revenue Bonds were retired in May 2008.

Under the provisions of GASB Statement 31, investments have been reported at fair value.

Investments consist of municipal obligations carried at fair value, determined by quoted market prices. Increases or decreases in fair value are recognized in the current period as investment gains or losses. Short-term investments are those with a maturity date of less than one year from the financial statement date.

***Estimates:***

The preparation of the financial statements in conformity with generally accepted accounting principles requires the use of management's estimates. The major estimates are unpaid claim liabilities.

***Unpaid Claims Liabilities:***

The Program establishes claim loss reserves for unpaid claims liabilities based on actuarial estimates of the ultimate cost of claims (including future allocated claim adjustment expenses) that have been reported but not paid or settled and that have been incurred but not reported. The liability includes the unallocated claims adjustment expense. The liabilities are based on the estimated ultimate cost of settling the reported and unreported claims, and claims reserve development including the effects of inflation and other societal and economic factors. Estimated amounts of subrogation and reinsurance recoverable on unpaid claims are deducted from the liability for unpaid claims. Estimated claims liabilities are recomputed periodically based on current reviews of claims information, experience with similar claims and other factors. Adjustments to estimated claims liabilities are charged or credited to expense in the periods in which they are made.

The Program is self-insured for workers' compensation claims to a maximum of \$500,000 per each occurrence. Losses in excess of \$500,000 are covered by reinsurance with a commercial carrier. Employer's liability claims are covered to a maximum of \$1,000,000 above the self-insured amount of \$500,000. During the fiscal year ended June 30, 2009 and 2008, the Program ceded \$240,712 and \$220,378 in premiums to reinsurers.



**MONTANA UNIVERSITY SYSTEM -  
WORKERS' COMPENSATION PROGRAM  
NOTES TO FINANCIAL STATEMENTS (Continued)  
June 30, 2009 and 2008**

**1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)**

***Cash and Cash Equivalents:***

Cash and cash equivalents consist of cash in checking accounts, specific investments held on behalf of the Program and pooled accounts with the Montana Board of Investments Short-Term Investment Program. For purposes of the statement of cash flows, the Program considers all highly liquid debt instruments purchased with initial maturities of three months or less to be cash equivalents.

***Premium Revenue:***

Premium rates are established by the Montana University System Self-Funded Workers' Compensation Program Committee based on anticipated premium needed as determined by the actuary. Premium rates are adjusted periodically based on inflation, claims experience, and other factors. Premiums are recorded as revenue in the period for which coverage is provided. Members may be subject to supplemental assessments in the event of deficiencies. The Program considers anticipated investment income in determining if a premium deficiency exists.

***Due from Component Unit:***

These amounts represent premium receivable from a component unit (Montana University System) of the State of Montana.

***Amortization of Bond Issuance Costs:***

Loan origination costs, which consist principally of underwriter's discount, legal and printing costs associated with the Series 2003 Bonds, are amortized using the straight-line method over the life of the bonds. The bonds were paid off during the fiscal year ended June 30, 2008.

**2. CASH AND INVESTMENTS**

Cash and cash equivalents at June 30 consist of the following:

|                                                   | <u>2009</u>          | <u>2008</u>         |
|---------------------------------------------------|----------------------|---------------------|
| Cash in bank                                      | \$ 836,757           | \$ 1,190,731        |
| Cash in Montana Board of Investments STIP Program | <u>11,396,754</u>    | <u>8,161,570</u>    |
| Totals                                            | <u>\$ 12,233,511</u> | <u>\$ 9,352,301</u> |

The following table presents the cost and the fair value of investments at June 30,

|                                | <u>2009</u>         |                     | <u>2008</u>       |                   |
|--------------------------------|---------------------|---------------------|-------------------|-------------------|
|                                | <u>Cost</u>         | <u>Fair Value</u>   | <u>Cost</u>       | <u>Fair Value</u> |
| Structured investment vehicles | <u>\$ 1,034,213</u> | <u>\$ 1,034,213</u> | <u>\$ 840,306</u> | <u>\$ 840,306</u> |

Effective June 30, 2005, the Program implemented the provisions of Governmental Accounting Standards Board (GASB) Statement No. 40 "Deposits and Investment Risk Disclosures". The investment risk disclosures are described in the following paragraphs.

**Legal and Credit Risk**

Credit risk is defined as the risk that an issuer or other counterparty to an investment will not fulfill its obligations.



**MONTANA UNIVERSITY SYSTEM -  
WORKERS' COMPENSATION PROGRAM  
NOTES TO FINANCIAL STATEMENTS (Continued)  
June 30, 2009 and 2008**

**2. CASH AND INVESTMENTS (Continued)**

Legal and Credit Risk (Continued)

In January 2007, the Board of Investments (the Board) purchased a \$25 million par issue of Orion Finance USA. In April 2007, the Board purchased two issues of Axon Financial Funding totaling \$90 million par and another \$25 million par issue of Orion Finance USA. As of June 30, 2007, these Structured Investment Vehicle (SIV) securities held in the STIP portfolio carried a combined amortized cost of \$139,991,131 representing 5.02% of the total portfolio. At the time of purchase and as of June 30, 2007, these four issues received the highest investment grade rating of AAA by Standard & Poors and Aaa by Moody's. As of June 30, 2008, these issues carried a D rating by Standard & Poors. On November 20, 2007, an insolvency event was declared by Axon Finance USA. Orion Financial Funding declared an insolvency event on January 14, 2008. On the January and April 2008 maturity dates, these securities matured at their amortized cost of \$140 million. The Board has determined that it is currently in the best interest of the STIP to continue to hold these securities in the investment portfolio. These SIV securities are currently generating cash to be applied to the securities.

The Montana University System - Workers Compensation Program's share of these investments as of June 30, 2009 and 2008 is \$1,034,213 and \$840,306, respectively. These are shown as long-term investments on the statement of net assets as of June 30, 2009 and 2008.

Concentration of Credit Risk

Concentration of credit risk is the risk of loss attributed to the magnitude of a government's investment in a single issuer. GASB 40 requires that a government entity disclose the amount invested in a separate issuer (except investments held in the U.S. government or investments guaranteed by the U.S. government) when that amount is at least 5% of total investments. As of June 30, 2008 and 2007 the Program had Structured Investment Vehicles that made up 100% of the total investments of \$1,034,213 and \$840,306, respectively:

Custodial Credit Risk

Custodial credit risk for investments is the risk that, in the event of the failure of the counterparty to a transaction, a government will not be able to recover the value of the investment or collateral securities that are in the possession of the outside party. Cash and money market funds are insured.

Information regarding the collateralization and risk of funds held by the Short Term Investment Pool (STIP) is available in the Board of Investment's comprehensive annual financial report. There is no regulatory oversight for the investment pool, and the pool does not have a credit quality rating. Participants' equity in the pool approximates the fair value of the underlying investments.

Interest Rate Risk

Interest rate risk is the risk that changes in interest rates will adversely affect the fair value of an investment. The Program investment policies do not formally address interest rate risk. In accordance with GASB Statement No. 40, the Program has selected the effective duration method to disclose interest rate risk.

GASB Statement No. 40 defines duration as a measure of the debt investment's exposure to fair value changes arising from changing interest rates. It uses the present value of cash flows, weighted for those cash flows as a percentage of the investment's full price. Effective duration makes assumptions regarding the most likely timing and amounts of variable cash flows arising from such investments as callable bonds, prepayments, and variable-rate debt.



**MONTANA UNIVERSITY SYSTEM -  
WORKERS' COMPENSATION PROGRAM  
NOTES TO FINANCIAL STATEMENTS (Continued)  
June 30, 2009 and 2008**

**3. RELATED PARTIES**

Certain employees of the campuses of the university system provide services to the Program at no charge. The value of such services has not been determined.

**4. UNPAID CLAIMS LIABILITIES**

As discussed in footnote 1, the Program establishes actuarial estimated unpaid claims liabilities. The estimated unpaid claims incurred but not reported and loss development liability have been adjusted to reflect the actuarial estimates of the ultimate cost of claims. The management of the Program has set the unpaid claims liability at the actuary's best estimate for 2009 and 2008. The following represents changes in the aggregate unpaid claims liabilities, excluding unallocated claim adjustment expense, for the Program for:

|                                                                           | <u>2009</u>         | <u>2008</u>         |
|---------------------------------------------------------------------------|---------------------|---------------------|
| Total present value of estimated unpaid claim losses at beginning of year | \$ 6,357,000        | \$ 5,503,000        |
| Changes in the estimated unpaid claim losses:                             |                     |                     |
| Provision for insured events of the current year                          | 2,922,000           | 2,693,000           |
| Increase (decrease) in provision for insured events of prior years        | <u>22,128</u>       | <u>(180,943)</u>    |
| Total incurred claims                                                     | <u>2,944,128</u>    | <u>2,512,057</u>    |
| Payments (including claims legal defense):                                |                     |                     |
| Claims paid attributable to insured events of current year                | 640,717             | 432,934             |
| Claims paid attributable to insured events of prior years                 | <u>927,411</u>      | <u>1,225,123</u>    |
| Total payments                                                            | <u>1,568,128</u>    | <u>1,658,057</u>    |
| Total present value of estimated unpaid claim losses at end of year       | <u>\$ 7,733,000</u> | <u>\$ 6,357,000</u> |

The estimated liability for workers' compensation claims as of June 30, consist of the following:

|                                                                 | <u>2009</u>         | <u>2008</u>         |
|-----------------------------------------------------------------|---------------------|---------------------|
| Estimated claims reported but unpaid                            | \$ 994,785          | \$ 855,695          |
| Estimated claims incurred but not reported and loss development | <u>6,738,215</u>    | <u>5,501,305</u>    |
|                                                                 | <u>\$ 7,733,000</u> | <u>\$ 6,357,000</u> |



**MONTANA UNIVERSITY SYSTEM - WORKERS' COMPENSATION PROGRAM  
CLAIMS DEVELOPMENT INFORMATION**

|    |                                                                                           | Fiscal and Policy Year Ended |              |              |              |              |              |
|----|-------------------------------------------------------------------------------------------|------------------------------|--------------|--------------|--------------|--------------|--------------|
|    |                                                                                           | 2004                         | 2005         | 2006         | 2007         | 2008         | 2009         |
| 1. | Required contribution and investment revenue                                              |                              |              |              |              |              |              |
|    | Earned                                                                                    | \$ 2,425,230                 | \$ 3,047,625 | \$ 3,708,977 | \$ 4,391,590 | \$ 4,997,477 | \$ 5,171,236 |
|    | Ceded                                                                                     | 151,286                      | 196,776      | 198,718      | 238,020      | 220,378      | 240,712      |
|    | Net earned                                                                                | 2,273,944                    | 2,850,849    | 3,510,259    | 4,153,570    | 4,777,099    | 4,930,524    |
| 2. | Unallocated expenses                                                                      | 227,267                      | 279,716      | 263,904      | 259,412      | 386,512      | 460,508      |
| 3. | Estimated incurred claims and expenses, end of policy year                                |                              |              |              |              |              |              |
|    | Incurred                                                                                  | 2,174,000                    | 2,366,000    | 2,453,000    | 2,600,000    | 2,693,000    | 2,922,000    |
|    | Ceded                                                                                     | -                            | -            | -            | -            | -            | -            |
|    | Net incurred                                                                              | 2,174,000                    | 2,366,000    | 2,453,000    | 2,600,000    | 2,693,000    | 2,922,000    |
| 4. | Net paid (cumulative) as of:                                                              |                              |              |              |              |              |              |
|    | End of policy year                                                                        | 551,749                      | 382,154      | 390,972      | 367,913      | 469,399      | 640,717      |
|    | One year later                                                                            | 1,019,751                    | 1,001,996    | 910,335      | 932,787      | 1,099,932    |              |
|    | Two years later                                                                           | 1,123,504                    | 1,227,600    | 1,254,242    | 1,092,644    |              |              |
|    | Three years later                                                                         | 1,147,508                    | 1,526,088    | 1,351,046    |              |              |              |
|    | Four years Later                                                                          | 1,165,362                    | 1,554,903    |              |              |              |              |
|    |                                                                                           | 1,210,361                    |              |              |              |              |              |
| 5. | Reestimated ceded claims and expenses                                                     | -                            | -            | -            | -            | -            | -            |
| 6. | Reestimated net incurred claims and expenses                                              |                              |              |              |              |              |              |
|    | End of policy year                                                                        | 2,174,000                    | 2,366,000    | 2,453,000    | 2,600,000    | 2,693,000    | 2,922,000    |
|    | One year later                                                                            | 2,174,000                    | 2,565,000    | 2,267,356    | 2,293,413    | 2,686,541    |              |
|    | Two years later                                                                           | 2,037,000                    | 2,459,000    | 2,510,000    | 2,412,000    |              |              |
|    | Three years later                                                                         | 1,830,000                    | 2,602,000    | 2,471,000    |              |              |              |
|    | Four years later                                                                          | 1,570,000                    | 2,622,000    |              |              |              |              |
|    | Five years later                                                                          | 1,499,000                    |              |              |              |              |              |
| 7. | Increase (decrease) in estimated net incurred claims and expenses from end of policy year | (675,000)                    | 256,000      | 18,000       | (188,000)    | (6,459)      | -            |

See the accompanying independent auditors' report on supplemental information





**Junkermier • Clark  
Campanella • Stevens • P.C.**

Certified Public Accountants and Business Advisors

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**REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING AND ON COMPLIANCE  
AND OTHER MATTERS BASED ON AN AUDIT OF FINANCIAL STATEMENTS  
PERFORMED IN ACCORDANCE WITH GOVERNMENT AUDITING STANDARDS**

To the Committee  
Montana University System - Workers' Compensation Program  
Helena, Montana

We have audited the financial statements of Montana University System - Workers' Compensation Program, (an enterprise fund of the State of Montana) as of and for the years ended June 30, 2009 and 2008, and have issued our report thereon dated December 1, 2009. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered Montana University System - Workers' Compensation Program's internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing our opinions on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of Montana University System - Workers' Compensation Program's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of Montana University System - Workers' Compensation Program's internal control over financial reporting.

A control deficiency exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect misstatements on a timely basis. A significant deficiency is a control deficiency, or combination of control deficiencies, that adversely affects the Montana University System - Workers' Compensation Program's ability to initiate, authorize, record, process, or report financial data reliably in accordance with generally accepted accounting principles such that there is more than a remote likelihood that a misstatement of the Montana University System - Workers' Compensation Program's financial statements that is more than inconsequential will not be prevented or detected by the Montana University System - Workers' Compensation Program's internal control.

A material weakness is a significant deficiency, or combination of significant deficiencies, that results in more than a remote likelihood that a material misstatement of the financial statements will not be prevented or detected by the Montana University System - Workers' Compensation Program's internal control.

Our consideration of internal control over financial reporting was for the limited purpose described in the first paragraph of this section and would not necessarily identify all deficiencies in internal control that might be significant deficiencies or material weaknesses. We did not identify any deficiencies in internal control over financial reporting that we consider to be material weaknesses, as defined above.



Compliance and Other Matters

As part of obtaining reasonable assurance about whether Montana University System - Workers' Compensation Program's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

However, we noted certain matters that we reported to management of Montana University System - Workers' Compensation Program in a separate letter dated December 1, 2009.

This report is intended solely for the information and use of the audit committee, management, others within the Montana University System - Workers' Compensation Program, and is not intended to be and should not be used by anyone other than these specified parties.

*Junkermier, Clark, Campanella, Stevens, P.C.*

Helena, Montana  
December 1, 2009





**MONTANA UNIVERSITY SYSTEM**  
**OFFICE OF THE COMMISSIONER OF HIGHER EDUCATION**

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(406) 444-6570 - FAX (406) 444-1469

December 1, 2009

Junkermier, Clark, Campanella, Stevens, P.C.  
Certified Public Accountants  
P.O. Box 1164  
Helena, Montana 59624

RE: Montana University System - Workers Compensation Program response

Dear Junkermier, Clark, Campanella, Stevens, P.C.

We have reviewed the draft audit report for the Montana University System - Workers Compensation Program. We are pleased that our Program meets accounting standards and that no recommendations for improvement were noted.

Sincerely,

A handwritten signature in black ink, appearing to read "Leah Tietz", is written over the typed name.

Leah Tietz  
Program Director





